

FINANCIAL STATEMENTS AND REPORT OF
INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS
WILLIAM NEWTON MEMORIAL HOSPITAL
DECEMBER 31, 2011 AND 2010

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WILLIAM NEWTON MEMORIAL HOSPITAL
MANAGEMENT'S DISCUSSION AND ANALYSIS
Years ended December 31, 2011 and 2010

Our discussion and analysis of the financial performance of William Newton Memorial Hospital (the Hospital) provides a narrative overview of the Hospital's financial activities for the years ended December 31, 2011 and 2010. Please read it in conjunction with the accompanying basic financial statements.

Financial highlights

The Hospital's net assets increased by \$1,057,230 or 7.4 percent in 2011, \$1,051,799 or 8.5 percent in 2010, and by \$982,004 or 8.0 percent in 2009.

The Hospital reported an operating income of \$1,088,745 in 2011, \$1,225,833 in 2010, and \$523,435 in 2009.

Using these financial statements

The Hospital's financial statements consist of three statements - a Balance Sheet; a Statement of Revenues, Expenses, and Changes in Net Assets; and a Statement of Cash Flows. These financial statements and related notes provide information about the activities of the Hospital, including resources held by or for the benefit of the Hospital, and resources restricted for specific purposes by contributors, grantors, and indenture agreements.

One of the most important questions asked about the Hospital's finances is, "Is the Hospital as a whole better or worse off as a result of the year's activities?" The Balance Sheet and the Statement of Revenues, Expenses, and Changes in Net Assets report information about the Hospital's resources and its activities in a way that helps answer this question. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. For purposes of these two statements, revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Hospital's net assets and changes in them. The Hospital's net assets - the difference between assets and liabilities - may be thought of as one way to measure its financial health, or financial position. Over time, increases or decreases in the Hospital's net assets are one indicator of whether its financial health is improving or deteriorating. Consideration must also be given to other nonfinancial indicators, such as changes in the Hospital's patient base and measures of the quality of service it provides to the community, as well as local economic factors, to assess the overall health of the Hospital.

The final required statement is the Statement of Cash Flows. This statement reports cash receipts, cash payments, and net changes in cash resulting from operations, investing, and financing activities. It provides answers to such questions as "Where did cash come from?", "What was cash used for?", and "What was the change in cash balance during the reporting period?"

WILLIAM NEWTON MEMORIAL HOSPITAL
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
Years ended December 31, 2011 and 2010

Assets, liabilities, and net assets

The Hospital's balance sheets as of the end of each of the last three years are summarized as follows:

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Assets			
Cash	\$ 6,534,777	\$ 4,760,301	\$ 4,029,478
Patient accounts receivable, net	4,362,572	4,364,179	3,871,612
Other current assets	<u>695,514</u>	<u>1,517,771</u>	<u>1,694,186</u>
Total current assets	11,592,863	10,642,251	9,595,276
Capital assets, net	<u>12,049,829</u>	<u>13,360,720</u>	<u>14,883,515</u>
Total assets	<u>\$ 23,642,692</u>	<u>\$ 24,002,971</u>	<u>\$ 24,478,791</u>
Liabilities and net assets			
Current liabilities	\$ 3,277,071	\$ 3,164,959	\$ 3,236,067
Noncurrent liabilities	4,969,220	6,498,841	7,955,352
Net assets	<u>15,396,401</u>	<u>14,339,171</u>	<u>13,287,372</u>
	<u>\$ 23,642,692</u>	<u>\$ 24,002,971</u>	<u>\$ 24,478,791</u>

The Hospital's cash balances have increased in each of the past three years as a direct result of positive operations and a reduction in the amount due from third-party payors. The number of days net revenue in net patient accounts receivable represented 65 days in 2011, 67 days in 2010, and 60 days in 2009. Other current assets decreased due to a decrease in the amount due from third-party payors which decreased by \$783,664 in 2011, as compared with 2010.

Capital assets decreased by \$1,310,891 in 2011 and decreased by \$1,522,795 in 2010. The change in capital assets will vary based on the timing of replacement in equipment and the annual provision for depreciation. In 2009, we completed a major renovation project that resulted in the complete refurbishment and furnishing of a nursing wing.

We utilize long-term leases or debt to finance major capital expenditures and try to maintain sufficient liquidity in our balance sheet to cover day-to-day operating expenses of the Hospital and to provide us flexibility in operating the Hospital. Our ratio of equity to total assets for the past three years was 65, 60, and 54 percent at December 31, 2011, 2010, and 2009, respectively. We did not enter into any new leases during 2011 or 2010.

WILLIAM NEWTON MEMORIAL HOSPITAL
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
Years ended December 31, 2011 and 2010

Operating results and changes in net assets

The Hospital's operating results and changes in net assets for each of the last three years are summarized as follows:

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Operating revenues	\$ 25,743,461	\$ 24,435,461	\$ 24,491,147
Operating expenses			
Salaries and benefits	13,706,644	13,179,631	13,513,582
Supplies and other	9,035,253	8,220,589	9,012,287
Depreciation	1,912,819	1,809,408	1,441,843
Total operating expenses	<u>24,654,716</u>	<u>23,209,628</u>	<u>23,967,712</u>
Operating income	1,088,745	1,225,833	523,435
Other changes in net assets	<u>(31,515)</u>	<u>(174,034)</u>	<u>458,569</u>
Increase in net assets	<u>\$ 1,057,230</u>	<u>\$ 1,051,799</u>	<u>\$ 982,004</u>

The first, and most significant, component of the overall change in the Hospital's net assets is its operating income - generally, the difference between net patient service revenue and the expenses incurred to perform those services. The Hospital's operating income decreased by \$137,088 in 2011 and increased by \$702,398 during 2010. The Hospital is designated as a critical access hospital and is generally reimbursed based on cost reimbursement principles by Medicare and traditional Medicaid beneficiaries.

Our operating margin decreased to 4.2 percent in 2011 as compared with 5.0 percent in 2010 and 2.1 percent in 2009. Total operating revenues increased by 5.4 percent in 2011 as compared to a marginal decrease in 2010. Operating revenues are impacted by volume of services provided, payor mix, level of charity care and uncompensated care, and expenses as this impacts our revenues associated with cost reimbursed services. As a not-for-profit hospital, we serve all patients who come to our Hospital, regardless of ability to pay. During 2011, 2010, and 2009 the Hospital wrote off \$1,665,211, \$1,399,482, and \$1,634,091 in charges related to bad debts or patients who qualify for charity care under our charity care policy. We receive some relief for the cost of uncompensated care as we qualify for Medicaid disproportionate share payments (DSH) which is designed to reimburse hospitals for the cost of uncompensated care related to both uninsured and Medicaid beneficiaries. Total payments received under the Medicaid DSH program in 2011, 2010, and 2009 were \$890,324, \$845,808, and \$731,084, respectively. The level of payments under this program is continually at risk due to budget constraints at both the federal and state levels of government.

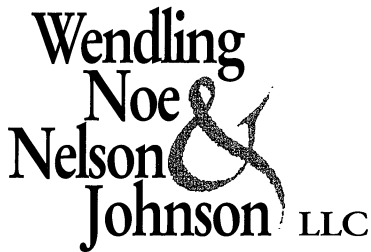
Operating expenses increased by 6.2 percent in 2011 as compared with 2010 and decreased by 3.2 percent in 2010 as compared to 2009. Significant items affecting the increase in operating expenses in 2011 as compared to 2010 were an increase in salaries and benefits for employees of \$527,013, an increase in radiation therapy contract services of \$360,000, and an increase in repairs and maintenance expense of \$225,000. We manage our expenses closely and attempt to hold them at or below normal inflationary pressures. Each year we evaluate our charge structure and adjust rates accordingly. These rate adjustments, however, do not impact net revenues proportionately, as the majority of third-party payors reimburse us for services based on either costs or set fee schedule rates that we have very little ability to control.

WILLIAM NEWTON MEMORIAL HOSPITAL
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
Years ended December 31, 2011 and 2010

Other changes in net assets were impacted in 2011 by the \$281,830 decrease in interest costs that are associated with long-term leases and the decrease of capital grants and contributions received in the amount of \$152,922. In 2010 there was an increase in interest cost of \$154,460 and a decrease in capital grants and contributions received of \$466,205.

The focus of Hospital management remains that of maintaining and growing utilization of Hospital services. Although the population living in our primary market area is not anticipated to fluctuate dramatically in the future, patient out-migration to other health care markets is a concern as some residents look outside our community for services. Our philosophy is to commit resources to maintain updated facilities and to invest in state of the art technology. We are also committed to offering programs and services that improve patient safety and promote a high level of quality care within the Hospital. Many factors, both internal and external, affect our ability to meet our goals. For example, to maintain or grow hospital utilization there is a requirement that the community have an adequate number and mix of primary care and specialty physicians. We monitor these numbers and continue to be proactive in the recruitment of physicians to our community.

This financial report is designed to provide a general overview of the Hospital's finances and to demonstrate the Hospital's accountability for the money it receives. If you have any questions about this report or need additional information, contact the Administration Office at 1300 East 5th Avenue, Winfield, Kansas 67156.



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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Trustees
William Newton Memorial Hospital

We have audited the accompanying financial statements of the business-type activity and discretely presented component unit of William Newton Memorial Hospital as of and for the years ended December 31, 2011 and 2010, which collectively comprise the Hospital's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the Kansas Municipal Audit Guide. These standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Hospital's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to previously present fairly, in all material respects, the financial position of the business-type activity and discretely presented component unit of William Newton Memorial Hospital as of December 31, 2011 and 2010, and their respective results of their operations, changes in their net assets, and cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Management's discussion and analysis on pages 1 through 4 is not a required part of the basic financial statements but is required supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Wendling Noe Nelson & Johnson LLC
Topeka, Kansas
June 14, 2012

WILLIAM NEWTON MEMORIAL HOSPITAL
BALANCE SHEETS
December 31,

ASSETS

	2011		2010	
	Hospital	Component unit	Hospital	Component unit
CURRENT ASSETS				
Cash and cash equivalents	\$ 6,534,777	\$ 145,533	\$ 4,760,301	\$ 518,437
Short-term investments		397,854		400,991
Patient accounts receivable, net of allowance for doubtful accounts of \$852,096 in 2011 and \$940,638 in 2010	4,362,572		4,364,179	
Other receivables	22,366	100,000	15,212	146,000
Inventories	280,680		311,803	
Prepaid expenses	215,820		230,444	
Estimated third-party payor settlements	176,648		960,312	
Total current assets	11,592,863	643,387	10,642,251	1,065,428
ASSETS LIMITED AS TO USE				
Principal of permanent endowments	-	443,250	-	243,250
CAPITAL ASSETS, net	12,049,829	-	13,360,720	-
	<u>\$ 23,642,692</u>	<u>\$ 1,086,637</u>	<u>\$ 24,002,971</u>	<u>\$ 1,308,678</u>

LIABILITIES AND NET ASSETS

CURRENT LIABILITIES				
Current maturities of capital leases	\$ 1,494,554	\$ -	\$ 1,572,137	\$ -
Accounts payable	484,126		367,761	
Salaries, wages, and related withholdings payable	573,916		518,903	
Accrued discretionary leave	724,475		706,158	
Total current liabilities	3,277,071	-	3,164,959	-
CAPITAL LEASES, net of current maturities	4,969,220	-	6,498,841	-
Total liabilities	8,246,291	-	9,663,800	-
NET ASSETS				
Invested in capital assets - net of related debt	5,586,055		5,289,742	
Temporarily restricted		441,845		631,072
Restricted nonexpendable permanent endowments		443,250		243,250
Unrestricted	9,810,346	201,542	9,049,429	434,356
	15,396,401	1,086,637	14,339,171	1,308,678
	<u>\$ 23,642,692</u>	<u>\$ 1,086,637</u>	<u>\$ 24,002,971</u>	<u>\$ 1,308,678</u>

The accompanying notes are an integral part of these statements.

WILLIAM NEWTON MEMORIAL HOSPITAL
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
Years ended December 31,

	2011		2010	
	Hospital	Component unit	Hospital	Component unit
Operating revenues				
Net patient service revenue	\$ 24,436,893	\$ -	\$ 23,629,155	\$ -
Other	<u>1,306,568</u>	<u>139,336</u>	<u>806,306</u>	<u>325,678</u>
Total operating revenues	<u>25,743,461</u>	<u>139,336</u>	<u>24,435,461</u>	<u>325,678</u>
Operating expenses				
Salaries and wages	11,112,949		10,689,919	
Employee benefits	2,593,695		2,489,712	
Supplies and other	9,035,253	355,192	8,220,589	481,193
Depreciation and amortization	<u>1,912,819</u>		<u>1,809,408</u>	
Total operating expenses	<u>24,654,716</u>	<u>355,192</u>	<u>23,209,628</u>	<u>481,193</u>
Operating income (loss)	<u>1,088,745</u>	<u>(215,856)</u>	<u>1,225,833</u>	<u>(155,515)</u>
Nonoperating revenues (expenses)				
Investment income	27,074	(6,185)	33,957	59,305
Interest expense	(437,838)		(719,668)	
Noncapital grants and contributions	146,770		126,653	
Other	<u>727</u>		<u>350</u>	
Total nonoperating revenues (expenses)	<u>(263,267)</u>	<u>(6,185)</u>	<u>(558,708)</u>	<u>59,305</u>
Excess of revenues over (under) expenses before capital grants and contributions	825,478	(222,041)	667,125	(96,210)
Capital grants and contributions	<u>231,752</u>		<u>384,674</u>	
Change in net assets	1,057,230	(222,041)	1,051,799	(96,210)
Net assets at beginning of year	<u>14,339,171</u>	<u>1,308,678</u>	<u>13,287,372</u>	<u>1,404,888</u>
Net assets at end of year	<u>\$ 15,396,401</u>	<u>\$ 1,086,637</u>	<u>\$ 14,339,171</u>	<u>\$ 1,308,678</u>

The accompanying notes are an integral part of these statements.

WILLIAM NEWTON MEMORIAL HOSPITAL
STATEMENTS OF CASH FLOWS
Years ended December 31,

	2011		2010	
	Hospital	Component unit	Hospital	Component unit
Cash flows from operating activities				
Receipts from and on behalf of patients	\$ 25,222,164	\$ -	\$ 23,356,276	\$ -
Payments to or on behalf of employees	(13,633,314)		(13,178,769)	
Payments to suppliers	(8,873,141)	(355,192)	(8,307,712)	(481,193)
Other receipts and payments	<u>1,299,414</u>	<u>185,336</u>	<u>798,485</u>	<u>494,678</u>
Net cash provided (used) by operating activities	<u>4,015,123</u>	<u>(169,856)</u>	<u>2,668,280</u>	<u>13,485</u>
Cash flows from noncapital financing activities				
Noncapital grants and contributions	<u>146,770</u>		<u>126,653</u>	
Net cash provided by noncapital financing activities	<u>146,770</u>	<u>-</u>	<u>126,653</u>	<u>-</u>
Cash flows from capital and related financing activities				
Purchases of capital assets	(601,928)		(303,613)	
Grants and contributions for capital	231,752		384,674	
Proceeds from sale of equipment	727		350	
Principal payments on capital leases	(1,607,204)		(1,409,810)	
Repayment of lines of credit			(50,000)	
Interest paid	<u>(437,838)</u>		<u>(719,668)</u>	
Net cash used by capital and related financing activities	<u>(2,414,491)</u>	<u>-</u>	<u>(2,098,067)</u>	<u>-</u>
Cash flows from investing activities				
(Increase) decrease in investments and permanent endowments		(237,868)		124,378
Investment income received	<u>27,074</u>	<u>34,820</u>	<u>33,957</u>	<u>4,313</u>
Net cash provided (used) by investing activities	<u>27,074</u>	<u>(203,048)</u>	<u>33,957</u>	<u>128,691</u>
Increase (decrease) in cash and cash equivalents	1,774,476	(372,904)	730,823	142,176
Cash and cash equivalents at beginning of year	<u>4,760,301</u>	<u>518,437</u>	<u>4,029,478</u>	<u>376,261</u>
Cash and cash equivalents at end of year	<u>\$ 6,534,777</u>	<u>\$ 145,533</u>	<u>\$ 4,760,301</u>	<u>\$ 518,437</u>

The accompanying notes are an integral part of these statements.

WILLIAM NEWTON MEMORIAL HOSPITAL
STATEMENTS OF CASH FLOWS - CONTINUED
Years ended December 31,

	2011		2010	
	Hospital	Component unit	Hospital	Component unit
Reconciliation of operating income to net cash provided (used) by operating activities				
Operating income (loss)	\$ 1,088,745	\$ (215,856)	\$ 1,225,833	\$ (155,515)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities				
Depreciation and amortization	1,912,819		1,809,408	
Provision for bad debts	1,092,899		1,014,292	
Changes in				
Patient accounts receivable	(1,091,292)		(1,506,859)	
Inventories	31,123		60,834	
Prepaid expenses	14,624		(96,286)	
Other receivables	(7,154)	46,000	(7,821)	169,000
Accounts payable and accrued expenses	189,695		(50,809)	
Estimated third-party payor settlements	783,664		219,688	
Net cash provided (used) by operating activities	<u>\$ 4,015,123</u>	<u>\$ (169,856)</u>	<u>\$ 2,668,280</u>	<u>\$ 13,485</u>
Supplemental schedule of noncash investing and financing activities				
Net change in unrealized gains on investments	\$ -	\$ (41,005)	\$ -	\$ 54,992

The accompanying notes are an integral part of these statements.

WILLIAM NEWTON MEMORIAL HOSPITAL

NOTES TO FINANCIAL STATEMENTS

December 31, 2011 and 2010

NOTE A - DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES

A summary of the significant accounting policies of William Newton Memorial Hospital consistently applied in the preparation of the accompanying financial statements follows.

1. Reporting entity

William Newton Memorial Hospital (Hospital) is owned by the City of Winfield, Kansas, (City) and is governed by a five-member Board of Trustees appointed by the City Commissioners. The Hospital, which was organized in 1927, is a 25-bed, not-for-profit general hospital located in Winfield, Kansas. The Hospital can sue and be sued, and can buy, sell, or lease real property.

The component unit discussed in Note A2 is included in the Hospital's reporting entity because of the nature and significance of its relationship with the Hospital.

2. Component unit

The financial statements include the financial data of the discretely presented component unit, William Newton Healthcare Foundation, Inc., (Foundation). The component unit is reported separately to emphasize that it is legally separate from the Hospital.

The Foundation is a legally separate not-for-profit corporation established in 2006 for the purpose of providing financial assistance to the Hospital and assisting the Hospital and others in the recruitment of physicians and other medical health care personnel to locate and practice in Winfield, Kansas. The Foundation is administered by a self-perpetuating Board of Directors which are appointed by the Hospital who is the sole voting member of the Foundation.

3. Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

4. Basis of accounting

The Hospital uses enterprise fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus. Based on Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the Hospital has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989, that do not conflict with or contradict GASB pronouncements.

WILLIAM NEWTON MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE A - DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES - Continued

5. Fair value of financial instruments

The carrying amount reported in the balance sheet for financial instruments including cash and cash equivalents, short-term investments, assets whose use is limited, accounts payable and other liabilities, settlements with third-party payors, and capital lease obligations approximate fair value.

6. Cash and cash equivalents

Cash and cash equivalents include all cash and highly liquid debt instruments with maturities of three months or less excluding any such amounts included in short-term investments or assets limited as to use.

7. Allowance for doubtful accounts

The Hospital provides for accounts receivable that could become uncollectible in the future by establishing an allowance to reduce the carrying value of such receivables to their estimated net realizable value. The Hospital estimates this allowance based on a percentage of revenue, the aging of its accounts receivable by type of payor, and its historical collection experience for each type of payor.

8. Inventories

Inventories are stated at cost as determined by the first-in, first-out method.

9. Assets limited as to use

Assets limited as to use include assets required to be retained in perpetuity by the contributors.

10. Capital assets

Capital assets (including assets recorded as capital leases) are stated at cost. Depreciation and amortization of capital assets are provided on the straight-line method over the estimated useful lives of the assets. The estimated lives used are generally in accordance with the guidelines established by the American Hospital Association.

The costs of maintenance and repairs are charged to operating expenses as incurred. The costs of significant additions, renewals, and betterments to depreciable properties are capitalized and depreciated over the remaining or extended estimated useful lives of the item or the properties. Gains and losses on disposition of capital assets are included in nonoperating gains and losses.

WILLIAM NEWTON MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE A - DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES - Continued

11. Grants and contributions

From time to time, the Hospital receives grants and contributions from individuals and private organizations. Revenues from grants and contributions are recognized when all eligibility requirements, including time requirements, are met. Grants and contributions may be restricted for specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as nonoperating revenues.

12. Accrued discretionary leave

Employees of the Hospital are entitled to paid time off depending on length of service and whether they are full-time or part-time. Upon resignation, termination or retirement from service with the Hospital, employees are entitled to payment for all accrued discretionary leave, up to an allowable maximum. The Hospital accrues these benefits as earned.

13. Net assets

Net assets of the Hospital are classified in four components. "Net assets invested in capital assets net of related debt" consist of capital assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. "Temporarily restricted" are net assets whose use has been limited by donors to a specific time period or purpose. "Restricted nonexpendable" are net assets equal to the principal portion of permanent endowments. "Unrestricted net assets" are remaining net assets that do not meet the definition of "invested in capital assets net of related debt," "temporarily restricted," or "restricted."

14. Operating revenues and expenses

The Hospital's statement of revenues, expenses, and changes in net assets distinguishes between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services, the Hospital's principal activity. Nonexchange revenues, including grants and contributions received for purposes other than capital asset acquisition, are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs.

15. Charity care

The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. The amount of charity care provided by the Hospital is disclosed in Note B.

WILLIAM NEWTON MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE A - DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES - Continued

16. Income taxes

The Hospital is exempt from federal income taxes pursuant to Section 115 of the Internal Revenue Code.

The Foundation is a not-for-profit corporation as described in Section 501(c)(3) of the Internal Revenue Code and is exempt from federal income taxes on its related income pursuant to Section 501(a) of the Code. Management is unaware of any uncertainties in income tax positions. Tax years ending on or after December 31, 2009, are subject to examination by taxing authorities.

NOTE B - NET PATIENT SERVICE REVENUE

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established charge rates. The amounts reported on the balance sheet as estimated third-party payor settlements consist of management's best estimate of the differences between the contractual amounts for providing covered services and the interim payments received for those services. A summary of the payment arrangements with major third-party payors follows:

Medicare - The Hospital is a critical access hospital for purposes of the Medicare program and is paid for most services rendered to Medicare beneficiaries under various cost reimbursement methodologies. Physician services are prospectively paid based on their respective fee schedules. The Hospital is paid for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits or reviews thereof by the Medicare administrative contractor. The Hospital's classification of patients under the Medicare program and the appropriateness of their admission are subject to an independent review by a peer review organization. The Hospital's Medicare cost reports have been audited or reviewed by the Medicare administrative contractor through December 31, 2009.

Medicaid - Acute care services rendered to Medicaid beneficiaries, other than those covered under HMO plans, are paid under provisions applicable to critical access hospitals. Payments to the Hospital under the critical access hospital provisions are based on cost reimbursement methodologies used by the Medicare program. Final settlement with the Medicaid program is based on a cost report after it is final settled by the Medicare program.

Blue Cross and Blue Shield - All services rendered to patients who are insured by Blue Cross and Blue Shield are paid on the basis of prospectively determined rates per discharge or discounts from established charges.

WILLIAM NEWTON MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE B - NET PATIENT SERVICE REVENUE - Continued

A summary of Hospital gross and net patient service revenue for the years ended December 31, 2011 and 2010, is as follows:

	<u>2011</u>	<u>2010</u>
Gross patient service revenue	\$39,466,653	\$36,312,567
Deductions from patient service revenue		
Third-party contractual adjustments	(13,986,934)	(11,886,456)
Medicaid DSH payments	890,324	845,808
Other discounts and allowances	(267,939)	(243,282)
Charity care	(572,312)	(385,190)
Provision for bad debts	<u>(1,092,899)</u>	<u>(1,014,292)</u>
Net patient service revenue	<u>\$24,436,893</u>	<u>\$23,629,155</u>

The Hospital estimates that the cost of providing charity care, based on overall cost to charge ratios obtained from the Hospital's cost reports was \$347,234 and \$250,909 for 2011 and 2010, respectively.

Revenue from the Medicare and Medicaid programs accounted for approximately 39 percent and 10 percent and 39 percent and 9 percent, respectively, of the Hospital's net patient service revenue during 2011 and 2010. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates could change by a material amount in the near term.

NOTE C - ASSETS LIMITED AS TO USE AND SHORT-TERM INVESTMENTS

Short-term investments and assets limited as to use, held by the Foundation, are carried at fair value which is determined based on quoted market prices in active markets, which are considered Level 1 inputs under GAAP. These assets are invested as follows and reported in the balance sheet under the following categories:

		<u>2011</u>	
	Cost	Unrealized gains (losses)	Fair market value
Equity mutual funds	\$ 428,740	\$ 7,812	\$ 436,552
Fixed income mutual funds	159,494	5,058	164,552
Certificates of deposit	<u>240,000</u>		<u>240,000</u>
	<u>\$ 828,234</u>	<u>\$ 12,870</u>	<u>\$ 841,104</u>
Short-term investments			\$ 397,854
Assets limited as to use			<u>443,250</u>
			<u>\$ 841,104</u>

WILLIAM NEWTON MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE C - ASSETS LIMITED AS TO USE AND SHORT-TERM INVESTMENTS - Continued

		2010	
	Cost	Unrealized gains (losses)	Fair market value
Equity mutual funds	\$ 254,546	\$ 50,732	\$ 305,278
Fixed income mutual funds	92,569	3,144	95,713
Certificates of deposit	243,250		243,250
	<u>\$ 590,365</u>	<u>\$ 53,876</u>	<u>\$ 644,241</u>
Short-term investments			\$ 400,991
Assets limited as to use			<u>243,250</u>
			<u>\$ 644,241</u>

NOTE D - CAPITAL ASSETS

Capital assets consist of the following:

	Balance December 31, 2010	Transfers and additions	Retirements	Balance December 31, 2011
Land	\$ 101,702	\$ -	\$ -	\$ 101,702
Land improvements	287,413			287,413
Buildings	20,066,451	15,242		20,081,693
Equipment	11,299,468	586,686	266,074	11,620,080
	<u>31,755,034</u>	<u>601,928</u>	<u>266,074</u>	<u>32,090,888</u>
Less accumulated depreciation and amortization				
Land improvements	269,727	2,789		272,516
Buildings	10,791,249	485,295		11,276,544
Equipment	7,333,338	1,424,735	266,074	8,491,999
	<u>18,394,314</u>	<u>1,912,819</u>	<u>266,074</u>	<u>20,041,059</u>
Capital assets, net	<u>\$13,360,720</u>	<u>\$ (1,310,891)</u>	<u>\$ -</u>	<u>\$12,049,829</u>

WILLIAM NEWTON MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE D - CAPITAL ASSETS - Continued

	Balance December 31, 2009	Transfers and additions	Retirements	Balance December 31, 2010
Land	\$ 101,702	\$ -	\$ -	\$ 101,702
Land improvements	287,413			287,413
Buildings	20,061,576	4,875		20,066,451
Equipment	11,394,989	281,738	377,259	11,299,468
	<u>31,845,680</u>	<u>286,613</u>	<u>377,259</u>	<u>31,755,034</u>
Less accumulated depreciation and amortization				
Land improvements	266,266	3,461		269,727
Buildings	10,302,958	488,291		10,791,249
Equipment	6,392,941	1,317,656	377,259	7,333,338
	<u>16,962,165</u>	<u>1,809,408</u>	<u>377,259</u>	<u>18,394,314</u>
Capital assets, net	<u>\$14,883,515</u>	<u>\$ (1,522,795)</u>	<u>\$ -</u>	<u>\$13,360,720</u>

The Hospital began a renovation of its obstetric wing and other upgrades of equipment in 2012. Total committed project costs are expected to be approximately \$1,600,000 during 2012.

NOTE E - CAPITAL LEASES

Capital lease obligations consist of the following:

	Date issued	Original amount	Interest rate	Outstanding balance 2011	2010
Capital lease obligations, collateralized by leased equipment with an amor- tized cost of \$741,173	Various dates	\$2,839,073	2.54% to 6.52%	\$ 629,978	\$1,286,655
Capital lease obligations, collateralized by buildings or building improvements with an amortized cost of \$6,964,418	Various dates	8,100,270	4.25% to 8.28%	5,833,796	6,784,323
Total capital leases				6,463,774	8,070,978
Less current maturities of capital leases				1,494,554	1,572,137
Capital leases, net of current maturities				<u>\$4,969,220</u>	<u>\$6,498,841</u>

WILLIAM NEWTON MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE E - CAPITAL LEASES - Continued

The following is a summary of changes in capital leases:

	Beginning principal outstanding	Additions to principal	Reduction of principal	Ending principal outstanding
2011 activity				
Capital leases	<u>\$ 8,070,978</u>	<u>\$ -</u>	<u>\$ 1,607,204</u>	<u>\$ 6,463,774</u>
2010 activity				
Capital leases	<u>\$ 9,480,788</u>	<u>\$ -</u>	<u>\$ 1,409,810</u>	<u>\$ 8,070,978</u>

Scheduled annual future minimum lease payments under capital leases are as follows:

Year	Principal	Interest	Total
2012	\$ 1,494,554	\$ 317,139	\$ 1,811,693
2013	1,145,503	227,691	1,373,194
2014	1,353,117	143,025	1,496,142
2015	122,800	102,627	225,427
2016	128,122	97,305	225,427
2017 - 2021	728,872	398,265	1,127,137
2022 - 2026	901,104	226,031	1,127,135
2027 - 2031	<u>589,702</u>	<u>36,547</u>	<u>626,249</u>
Total	<u>\$ 6,463,774</u>	<u>\$ 1,548,630</u>	<u>\$ 8,012,404</u>

NOTE F - DEFINED BENEFIT PENSION PLAN

Plan description. The Hospital participates in the Kansas Public Employees Retirement System (KPERS), a cost-sharing multiple-employer defined benefit pension plan as provided by K.S.A. 74-4901, et. seq. KPERS provides retirement benefits, life insurance, disability income benefits, and death benefits. Kansas law establishes and amends benefit provisions. KPERS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to KPERS (611 S. Kansas Avenue, Topeka, Kansas 66603-3869) or by calling 1-888-275-5737.

Funding policy. K.S.A. 74-4919 establishes the KPERS member-employee contribution rate at 4 percent of covered salary for an employee first employed before July 1, 2009. K.S.A. 74-49,210 establishes the KPERS member-employee contribution rate at 6 percent of covered salary for an employee first employed on or after July 1, 2009. The employer collects and remits member-employee contributions according to the provisions of Section 414(h) of the Internal Revenue Code. State law provides that the employer contribution rate be determined annually based on the results of an annual actuarial valuation. KPERS is funded on an actuarial reserve basis. State law sets a

WILLIAM NEWTON MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE F - DEFINED BENEFIT PENSION PLAN - Continued

limitation on annual increases in the contribution rates for KPERS employers. The employer rate established by statute at December 31, 2011 and 2010, is 7.49 percent and 6.89 percent. The Hospital employer contribution to KPERS for the year ended December 31, 2011 and 2010, was \$806,077 and \$689,073, equal to the statutory required contributions for the year.

NOTE G - OPERATING LEASES

The Hospital leases equipment under operating leases with related rentals charged to operations as incurred. Total rent expense for 2011 and 2010 was approximately \$224,000 and \$271,000, respectively.

NOTE H - RISK MANAGEMENT

The Hospital is insured for professional liability under a comprehensive hospital liability policy provided by an independent insurance carrier with limits of \$200,000 per occurrence up to an annual aggregate of \$600,000 for all claims made during the policy year. The Hospital is further covered by the Kansas Health Care Stabilization Fund for claims in excess of its comprehensive hospital liability policy up to \$800,000 pursuant to any one judgment or settlement against the Hospital for any one party, subject to an aggregate limitation for all judgments or settlements arising from all claims made in the policy year in the amount of \$2,400,000. The policy provided by an independent insurance carrier also provides for umbrella liability in excess of the underlying limits set forth above in the amount of \$1,000,000 per occurrence with an aggregate in any one policy year of \$1,000,000. All coverage is on a claims-made basis. The Hospital renewed this coverage in January 2012 for a one-year term.

NOTE I - DEPOSITS WITH FINANCIAL INSTITUTIONS

Kansas statutes authorize the Hospital, with certain restrictions, to deposit or invest in open accounts, time deposits, certificates of deposit, repurchase agreements, the State Treasurer's municipal investment pool, and U.S. Treasury bills and notes. Statutes also require that financial institutions pledge securities with a market value equal to total deposits, in excess of F.D.I.C. coverage at any given time, and the securities pledged be deposited with a Kansas state or national bank or trust company, the Federal Reserve Bank, the Federal Home Loan Bank, or the Kansas State Treasurer.

WILLIAM NEWTON MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE I - DEPOSITS WITH FINANCIAL INSTITUTIONS - Continued

The carrying amount of the Hospital's deposits with financial institutions including repurchase agreements was \$6,534,777 and the bank balance was \$6,652,990 at December 31, 2011. The bank balance is categorized as follows at December 31, 2011:

Amount insured by the F.D.I.C., or collateralized with securities held by the Hospital in the Hospital's name	\$ 820,903
Uncollateralized (collateralized with securities held in safekeeping under joint custody receipts by an authorized depository other than the pledging financial institution's trust department but not in the Hospital's name)	<u>5,832,087</u>
	<u>\$ 6,652,990</u>

NOTE J - CONCENTRATION OF CREDIT RISK

The Hospital is located in Winfield, Kansas. The Hospital grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors is as follows:

	<u>2011</u>	<u>2010</u>
Medicare	29%	31%
Medicaid	9	8
Blue Cross	16	12
Commercial insurance	20	15
Self-pay	<u>26</u>	<u>34</u>
	<u>100%</u>	<u>100%</u>

NOTE K - COMMITMENTS AND CONTINGENCIES

The Hospital sponsors a self-funded Employee Group Benefit Trust (EGBT) for the benefit of its employees. The Hospital deposits funds into the EGBT monthly and pays claims submitted on behalf of its employees. The EGBT purchases reinsurance to cover claims in excess of specific limits. Since the assets of the EGBT are not controlled by the Hospital and are held for the sole benefit of its employees, the assets and related liabilities are not included in the Hospital's financial statements. At December 31, 2011, the EGBT had total assets of \$449,777 with which to pay claims.

WILLIAM NEWTON MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2011 and 2010

NOTE K - COMMITMENTS AND CONTINGENCIES - Continued

In addition to the risk disclosed elsewhere in these financial statements and notes thereto, the Hospital is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Hospital purchases commercial insurance for these risks. Settled claims have not exceeded this commercial coverage in any of the past three years.

NOTE L - RELATED PARTY TRANSACTIONS

William Newton Memorial Hospital Foundation is a component unit of the Hospital (see Note A2). The Hospital employs the Foundation director and staff and provides office space to the Foundation at no cost. The Foundation also periodically transfers funds to the Hospital to support the Hospital's mission. During 2011 and 2010, the Foundation transferred \$332,353 and \$465,424 to the Hospital for the purchase of equipment and capital improvements to patient rooms.

NOTE M - RESTRICTED NET ASSETS

When a donor specifies the purpose of a contribution, the contribution and related income is recorded as either temporarily restricted or permanently restricted according to the donor's request. If the Foundation receives a gift that does not specify a restriction, the Foundation records the gift as unrestricted.

The Foundation's net assets include permanent endowments, the income from which is to accumulate to enable the Foundation to provide continuing support to the Hospital. As required by generally accepted accounting principles, net assets associated with the endowment funds are classified and reported based on the existence of donor-imposed restrictions.

The Board of Trustees has interpreted the Kansas Uniform Prudent Management of Institutional Funds Act (UPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Foundation classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowments, (b) the original value of subsequent gifts to the permanent endowments, and (c) accumulations to the permanent endowments made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the funds. The remaining portion of the donor-restricted endowment funds is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Board of Trustees in a manner consistent with the standard of prudence prescribed by UPMIFA.

It is the policy of the Board to manage its investment in a prudent manner consistent with good stewardship, yet striving to enhance its return on the available funds. To assist in accomplishing this objective, the Board has established an asset allocation policy, engages a professional investment advisor, and monitors the investments and investment returns.

WILLIAM NEWTON MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE M - RESTRICTED NET ASSETS - Continued

If the fair value of assets associated with donor-restricted funds falls below the level that the donor or UPMIFA requires the Foundation to retain as permanently restricted, such deficiencies are reported in unrestricted net assets. At December 31, 2011, no such deficiencies existed.

NOTE N - SUBSEQUENT EVENTS

Management has reviewed subsequent events through the date of the independent accountant's report, which is the date the financial statements were available to be issued.